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Faculty of Economics

CEWP 05/2018

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by
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New European Banking Governance and Crisis of Democracy:

Insights from the European post-socialist periphery

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Version: 21.11.2018

In this article, we argue that the post-crisis banking governance framework of the European Union, not only severely constrains peripheral member states' governments in their policy choices, but more profoundly rearranges their government institutions in a way to restrict sovereign banking policy formation. Furthermore, amending the most dominant narratives of the EU's impact on national banking policy, which point either at the role of the Economic and Monetary Union, or the Banking Union, we argue that it is also and most profoundly the organization of the Single Market and the various changes made to its architecture that influence EU member states' banking policy. Finally, and most importantly, building on the case study of the post-crisis bank restructuring in Slovenia we reinvigorate the debate on the contribution of economic policy to the crisis of democracy in the EU by demonstrating the strong effect of the European banking governance on decreasing democratic oversight of banking policy in member states.

JEL: F55, E58, E62, E36

Keywords: Slovenia, banking, state aid, fiscal policy, central bank, Banking Union

Introduction

In Europe, the framework of bank regulation and supervision has undergone formidable changes since the global financial crisis. Bank and state ties have been loosened by the

introduction of the Banking Union (BU) (Epstein, 2017). The role of the European Central Bank (ECB) has been widened to policy areas previously unknown to central banking (Chang, 2018; McPhilemy, 2016). The European Semester and the Fiscal Compact increased the European Commission's (EC) surveillance over member states' fiscal policy (Verdun & Zeitlin, 2018) and as such over their banking policy as well. The post-crisis remodeling of the governance of the European Union (EU) enhanced multi-level polity of member states (Scharpf, 1999) and their "institutionally incomplete character" (Deeg & Jackson, 2007, p. 154). In turn, the uneven redistribution of state policy-making competencies between the European institutions and member states have been identified by a number of researchers as one of the causes behind the weakening of European democracy during the crisis (Durand & Keucheyan, 2015; Scharpf, 2014; Streeck, 2014, pp. 97-164).

This article contributes to the debate on the relationship between the post-crisis European architecture and the crisis of democracy by analyzing the politics of bank restructuring in member states on the EU's periphery. Banks are central to policy-making in market economies (Calomiris & Haber, 2014). They are not only the key institutions for the well-functioning of the modern economy, but they also act as important policy tools for governments to determine the allocation of credit among differently located economic actors, promote regional growth, decrease unemployment, etc. (Gerschenkron, 1962; Zysman, 1983). However, they are also sources of uncertainty, risk, and instability that can threaten the smooth functioning of the economy. As Epstein (2014) succinctly argued they are assets as well as liabilities, that must be carefully regulated. Politics of bank regulation, in turn, concern the whole of society, due to the banks' systemic interconnectedness with the economy. After the current financial crisis, bank regulations have been massively redesigned

at multiple levels within the EU (De Rynck, 2016; Epstein, 2017; Howarth & Quaglia, 2016; Schelkle, 2017).

Up until now, the most systemic account on the effects of the new European banking regulations on member states was provided by Epstein (2017). According to her, the BU transformed “bank-state ties” and significantly downsized the Eurozone member states' discretion over economic policy. We bring her account into a dialogue with the literature on the reorganization of the European market governance structure and the crisis of democracy (Scharpf, 2011; Streeck & Schäfer, 2013). We do so by enlarging Epstein's focus to include not only the relations between the European and national authorities but also other political processes and actors such as the European state transformation and democracy, i.e. the relationship between national authorities and citizens. Moreover, by looking at the BU only, Epstein (2017) adopted a narrower definition of what accounts as a new European banking regulatory and supervisory framework. We widen this focus, because national banking systems interact with other institutions and macroeconomic policies, as persuasively demonstrated by Streeck (2009). A wider array of regulations, and not only the BU, should be considered in order to understand the multi-fold impact of the post-crisis European banking governance on the crisis-provoked bank restructuring.

Thus, we propose a new conceptualization of the emerging European governance structure and introduce the term New European Banking Governance (NEBG). NEBG is more encompassing than the BU. It includes (1) regulations of state aid, (2) fiscal coordination, (3) central banking, and (4) BU. NEBG impacts political relations of member states through a complex mechanism of political coordination of banking policy that not only takes place at different levels but also produces uneven impacts on state institutions and the bargaining

power of institutional actors. On the one hand, the NEBG relocates significant decision-making powers from member states to the supranational level. On the other hand, this supranationalization of member states' banking policy simultaneously increases decision-making abilities and powers of the executive and central banking institutions at the national level at the expense of those related to democratic policy-making. In addition, NEBG's uniform macroeconomic design achieves only a limited economic efficiency. Nonetheless, rejecting contestation of the NEBG-shaped bank restructuring is made easier due to the responsible institutions' increased decision-making powers. NEBG, therefore, undermines the legitimacy of both European and domestic institutions, and hence, contributes to the weakening of the European multi-governance system as well. While it would be misleading to put all the responsibility for such an outcome on European banking governance, decreased democratic oversight in banking is critical for developments in the whole of society because of the systemic importance of the banking sector for the functioning of the economy.

Therefore, our argument also differs from Epstein's (2017) in that we see that the NEBG's impact on member states simultaneously constraints and enables domestic institutions and actors. In addition, we emphasize that these changes do not impact EU member states evenly. As it has been shown in relation to the BU and EMU, the more powerful member states such as Germany (Donnelly, 2018) or France (Schild, 2018) have a very different interaction with the common regulatory framework than countries in the EU's periphery. By relying on the concept of the NEBG and considering European statehood as a form of multi-level polities (Scharpf, 1999, 2014), we demonstrate that NEBG plays a significant role in the systemic weakening of democratic practices in member states on the periphery. The European periphery has younger and weaker democratic institutions, especially in post-socialist Eastern Europe, than the West (Bohle & Greskovits, 2012; Holman, 2004). Peripheral member states

were more severely hit by both the financial crisis and the sovereign debt crisis than core countries, especially the Southern periphery (Becker & Jäger, 2012). Finally, core countries and businesses in core countries have significantly more important structural and lobby power and are more capable to negotiate preferential treatment with European institutions in relation to the enforcement of common rules.

Slovenia is a particularly insightful case to study this process. This is because Slovenia has relatively new democratic institutions similar to other small, eastern Eurozone member states such as Slovakia or the Baltic States. However, the country also differs from other Eastern European countries in that up until the crisis it preserved its economic nationalist welfare capitalism and neo-corporatist regime (Bohle & Greskovits, 2012; Lindstrom, 2015). In addition, Slovenia was also much harder hit by the crisis than most eastern member states. In fact, Slovenia shares with Greece, Portugal, Spain, Italy, and Cyprus both the experience of the sovereign debt crisis and European institutions' response to this crisis (Kržan, 2014). However, the Slovenian government succeeded to recapitalize domestic banks without demanding the Troika's financial assistance (Podvršič, 2018). Therefore, the study of bank restructuring in Slovenia allows the filtering out of the influence of the International Monetary Fund (IMF) and to bring forward the democracy constraining effect of the new European regulatory framework. Hence, the Slovenian experience with NEBG is to some extent unique. However, because Slovenia features all the scope conditions under which NEBG's impact is heightened on the periphery, it is the perfect laboratory to study this process. Although the findings generalizability remains limited, the Slovene case adds a critical variant to the impact of NEBG on peripheral member states.

While there are many studies on the erosion of the Slovenian democratic corporatism during the crisis, emphasizing the importance of the external actors' pressures (Guardiancich, 2016; Lindstrom, 2015; Stanojević, Kanjuo Mrčela, & Breznik, 2016), no attempt was made to make a sectorial account and to explore systematically the role of the new European regulations on Slovenian policy-making. By studying policy-making over the banking crisis in Slovenia through the NEBG conceptual framework, we show that the European governance structures over the banking sector structurally narrowed domestic sovereign and democratic policy-making space.

The article is organized as follows. The first section provides a theoretical background and explains the main features of the NEBG. The following section analyses bank restructuring in Slovenia. We conclude that regardless of their macroeconomic effects, the regulations framing member states' banking policies contribute to shrinking democratic accountability of policy-making institutions on the national as well as European levels.

European Multi-level Polity and the Crisis of Democracy

At the turn of 2010, the European Commission launched a complete new set of regulations under the name of the New European Economic Governance (NEEG) (Degryse, 2012) in order "to protect the euro as the most important asset of the EU" (European Commission, 2010), as Barroso succinctly explained. During the following years, the NEEG became more and more sophisticated and was complemented in 2012 with the proposal for establishing the BU (for more see below).

While some authors have considered these changes as being in line with past institutional practices (Verdun, 2015), others have pointed to a significant remodeling of European political relations. This has involved broadened discretionary powers of the EC (Bauer & Becker, 2014); the intensification of intergovernmental decision-making (Epstein & Rhodes, 2016; Fabbrini, 2017; Schimmelfennig, 2015); the expansion of supervising capacities and politicization of the ECB (da Conceição-Heldt, 2016); the policy-making influence of the representatives of the leading financial and corporate multinationals (van Apeldoorn, 2013); and a new collaboration between the European bodies and the IMF, which started with the lending packages to different post-socialist countries at the end of the 2000s (Lütz & Kranke, 2014; Piroška, 2017).

Thus, with the post-crisis European architecture, the relationships between the EU and the states, as well as within the states have been altered – although significant national differences remain relative to the countries’ membership status, socio-economic situations and political constellation. Various scholars came to agree that the chosen macroeconomic policies, combining austerity measures with further economic liberalization deepened and prolonged the European economic hardship and created new political and economic divides between the member states (Boyer, 2012; Bruszt & Vukov, 2017; De Grauwe & Ji, 2013; Flassbeck & Lapavistas, 2015; Stockhammer, 2016). In addition, by interfering simultaneously in member states’ fiscal policy, including budgets over wage, health and education systems, competition rules and monetary regimes, these new regulations have significantly reduced member states’ macroeconomic capacities (Stockhammer, 2016; Streeck & Schäfer, 2013).. In turn, reduced macroeconomic policy scope narrowed down fiscal democracy. This is because, “democracy has not only formal prerequisites – equal voting rights – but also substantive prerequisites – policy choice and autonomy in government budgetary choice” (Genschel & Schwarz, 2012).

As a consequence, the top-down one-size-fits-all macroeconomic policies, irrespective of deep variations between the crisis situations among the European economies, undermined democratic policy-making and institutions in member states and provided limited economic efficiency (Streeck & Mertens, 2013).

The new wave of supranational integration and deepened coordination has impacted national institutions in an uneven way, due to the asymmetrical nature of European governance (Scharpf, 1999). It reinforced the bargaining powers and the ability to decide upon the institutional changes of the executive and those institutions linked to finance (cf. Durand & Keucheyan, 2015). During the Eurozone crisis, the ECOFIN Council, made up of the economics and finance ministers from all EU member states and the European Council of the Head of the Eurozone governments became the key decision-making bodies (Bonefeld, 2016; Keucheyan & Durand, 2015; Streeck, 2015). In contrast, no attempt was made to reinforce the powers of the European Parliament, with no right of legislative initiative or power to change the EU treaties (Streeck, 2015). Moreover, already before the crisis, the European social dialogue was limited to specific domains and formed a “non-binding social partnership forum” (Horn, 2012, p. 583). Under the new European architecture, labor was even more sidelined (Horn, 2012). “Social issues are not addressed for their own sake but, rather, operate as adjustment variables under the heading of financial stability, macro-supervision of fiscal policy and competitiveness” (Durand & Keucheyan, 2015, pp. 11-12).

This is why Streeck (2015, p. 366) underlined that “[e]uropeanization today is by and large identical with a systematic emptying of national democracies of political-economic content”. According to Oberndorfer (2015), the new European supranational regime tends to replace the antagonism between the EU and the nation-state with the antagonism between (representative)

democracy and the ensemble of state institutions that the new European regulations connected into a dense policy making sheltered from democratic supervision. A number of scholars have substantiated these claims by exploring the weakening of democracy in various member states, especially in Hungary (Tóth, 2015) and in the so-called PIIGS countries (Matthijs, 2017).

To contribute to the debate on the new European architecture and the crisis of democracy this article makes an account on the banks restructuring. Finance and banking have been regarded as a key sector for governments' economic policy formation (Gerschenkron, 1962; Zysman, 1983). Notwithstanding, governments' ability to shape financial markets has been decreasing ever since the liberalization wave of the 1980s (Haggard, Lee, & Maxfield, 1993; Kurzer, 1993; Loriaux, 1996; Pérez, 1997). This change has been linked not only to the government's weakening capacity to influence the organization of credit (Germain, 1997), but also relatedly to the weakening public control of the redistributive consequences of the regulatory arrangements (Pauly, 1997). Within the EU, two changes had weakened the influence of governments over finance in the 1990s. First, the Maastricht Treaty in 1992 laid the basis for a single monetary policy, established a common monetary authority, and prescribed restrictive macroeconomic targets for member states. In addition, European banking regulations developed toward a tighter supranational integration, but with profound subsidiarity concerns, while becoming increasingly diffused among multiple actors, such as private banks, rating agencies, law firms and independent government agencies as well as international organizations and powerful states (Sinclair, 1994). In the meantime, the nature of banking has been transformed with a shift from bank-based to market-based banking, which had important implications for the extent of government control (Hardie, Howarth, Maxfield, & Verdun, 2013). Parallel to member states' major efforts to liberalize and re-regulate banking, however,

banking nationalism also flourished and western European member states implemented regulations to strengthen national banks (Epstein & Rhodes, 2016).

The global financial crisis has painfully revealed the weakness of the European banking regulatory infrastructure. Post-crisis, researchers focused on the reasons behind the decision to preserve the common currency (Schelkle, 2017) and national governments' agreement to delegate a substantial part of decision-making power over banks to the supranational level (Epstein & Rhodes, 2016; Lombardi & Moschella, 2016). In addition, the characteristics of the BU have been discussed (Donnelly, 2018; Howarth & Quaglia, 2016), as well as the conditions under which non-Eurozone member states would join the BU (Méró & Piroška, 2016; Spendzharova, 2014; Spendzharova & Emre Bayram, 2016). However, fewer attempts have been made to link the new European banking governance to the actual restructuring of banking in member states and to the weakening of democratic oversight of these policies.

Instead, there is a vivid discussion on the impact of the narrower EMU design on member states' abilities to pursue an efficient macroeconomic policy. Scharpf (2011, p. 11), for instance, has argued that the EMU "has removed crucial instruments of macroeconomic management from the control of democratically accountable governments." Reviewing alternations to input and output legitimacies, his conclusions are very strong: for peripheral EU member states, such as Greece, the only viable option both for efficient economic policy and preserving substantial democracy is to leave the Eurozone. While many scholars working on the asymmetrical linkages between the European economies (Becker & Jäger, 2012; Flassbeck & Lapavistas, 2015) confirm Scharpf (2011)'s claim, his proposition was contested by Mabbett and Schelkle (2015). Pointing to the experience of non-Eurozone member states Hungary and Latvia, they argued – following insights from Epstein (2013) – that it was not

the opportunity to devalue the local currency, but foreign banks' willingness to maintain pre-crisis credit exposures that explained the success of national governments' crisis management. This point is well taken. However, the accounts on the macroeconomic efficiency of the European regulations should be complemented by the analysis of the impact of crisis management on the democratic character of policy-making in these countries.

Another important contribution to the relationship between the European supranational regulations and democracy crisis has been provided by Epstein (2017). According to her, BU has transformed "bank-state ties" and significantly downsized the Eurozone member states' discretion over economic policy. Epstein (2017)'s account on the BU is therefore valuable for understanding the EU banking regulations not only in terms of technical-economic adjustments but also as mechanisms that modify states' functioning as such. This article adds a new political dimension of state transformation into the analysis, i.e. citizens and democracy, which is rather unexplored in Epstein's account. Moreover, Epstein (2017) adopts a narrow definition of what accounts as a new European banking regulatory and supervisory framework. Because national banking systems interact with other institutional forms of national economies and macroeconomic policies one should consider a wider array of regulations to understand the multi-fold impact of the new European banking regulations in member states.

New European Banking Governance

Hence, it is suggested to introduce a new conceptualization of European banking governance. NEBG can be considered as a subset of the NEEG framework and is based on four regulatory pillars: (1) state aid policy, (2) fiscal coordination, (3) central banking, (4) BU. Member

states' banking policy falls within all four domains to various degrees depending on the integration of the country into European structures.

Since the late 1980s, state-aid rules have probably been the most important tools in the hand of the EC to push member states towards liberalization (Wigger, 2015). After the collapse of Lehman Brothers, the Directorate General for Competition (DG-COMP) launched six key directives to regulate state aid to the banking sector: the Banking Communication (October 2008), the Recapitalization Communication (December 2008), the Impaired Assets Communication (February 2009), the Restructuring Communication (July 2009), the Prolongation Communication (December 2010) and the New Banking Communication (August 2013). These directives reinforced the already existing principles regulating Single Market state aid rules to the corporate sector. European policy regarding member states' rescue and restructuring of banks has progressively become more restrictive, especially in the case of the recapitalization of banks considered being at risks of solvency and therefore requiring a larger public aid. National authorities became obliged to provide far-reaching restructuring plans, detailing also the changes of management and corporate governance of the rescued banks in order to minimize state involvement in the future. In parallel, the EC and external experts gained powers to check and confirm the evaluation of banks' assets, made by national authorities. Finally, burden-sharing requirements became stricter as well and moved from the so-called bail-out approach, favoring the participation of national governments, towards the so-called bail-in approach that has required the participation of shareholders and subordinated debt holders in banks' rescue. Note that after 2012, the state aid to banks regulations overlapped with the provisions constituting the BU (see below).

Until the outbreak of the Eurozone crisis, fiscal policy fell mainly under member states' jurisdiction and remained flexible with regards to member states' specific circumstances. However, with the adoption of the European Semester (May 2010), Six-Pack (December 2011) and Two-Pack (May 2013) provisions, the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG, March 2012), signed by all EU member states except the UK, the Czech Republic and Croatia, the competencies of the EC, especially the Directorate General for Economic and Financial Affairs (DG-ECFIN) (Keucheyan & Durand, 2015) has increased significantly. The DG-ECFIN was accorded the right to examine, in collaboration with the Council of the EU, ex ante, give an opinion, and demand revision on member states' draft budgets as provided within the annual Stability and Convergence Programs; gained a policy toolkit to control and monitor the implementation of reform measures as elaborated in the annual National Reform Programs; and launch the procedure to penalize member state financially if the reforms are not implemented correctly. Overall, the fiscal policy reform has impacted member states' banking policies in two ways. First, in peripheral states whose banks accumulated significant burdens prior to the crisis, fiscal restrictions aggravated the debt ratio, especially if detained by the private sector. Second, the DG-ECFIN gained power, with a reference to budgetary concerns, to overwrite significant elements of a member state's banking policy such as taxing banks, buying and selling banks, rescuing banks, or setting up regulatory forbearance, etc.

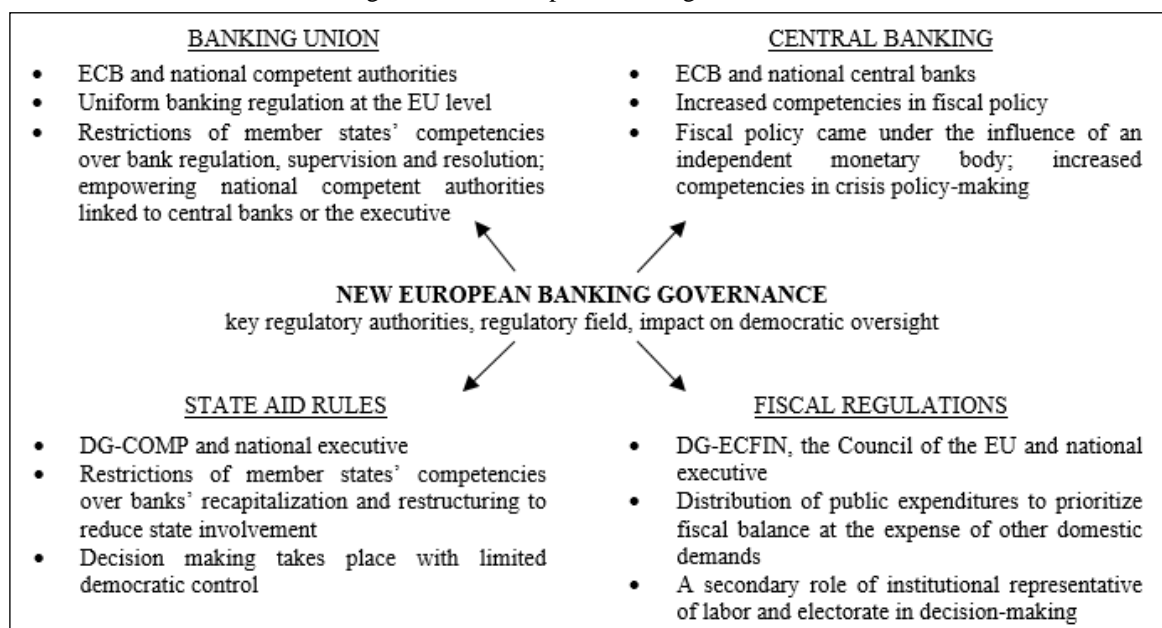
Up to the crisis, central banking was narrowly defined to achieve only monetary stability, while the stability of the economy including that of the financial sector was to be achieved through the adherence to strict macroeconomic targets (Chang, 2018; Johnson, 2016; Mishkin, 2013). This has profoundly changed post-crisis and the ECB and other central banks now take on the responsibility for the supervision of the financial sector. However, the ECB

and a few other central banks went further and developed competencies in a number of other domains allowing central banking authorities to become actively engaged in member states' macroeconomic policy-making with domestic fiscal and redistributive consequences (Högenauer & Howarth, 2016). During the first years of the crisis, the ECB provided liquidity to private financial institutions and bought government bonds on secondary markets (Keucheyan & Durand, 2015, pp. 34, 35). After 2012, however, the intensification of the peripheral sovereign debt crisis pushed the bank to expand its balance sheet more substantially (Flassbeck & Lapavistas, 2015). As such, the ECB initially refused to act as a lender of last resort, which would have reduced pressures on the troubled Eurozone periphery with no monetary sovereignty (Gabor 2012). It was only after 2012, that the ECB committed itself to buying government bonds within the so-called Outright Monetary Transaction (OMT) program (August 2012) (Stockhammer, 2016). However, the OMT has also granted the ECB the right to put pressure on national governments with large public debt by allowing yields on government bonds to increase or by inducing such increases. In addition, as a member of the Troika, the ECB regularly intervened politically in the crisis management of member states and provided advice to governments (Keucheyan & Durand, 2015; Streeck, 2015).

With the introduction of the BU, the ECB has assumed explicit rights to supervise, regulate and restructure banks in member states. The BU currently consists of the Capital Requirements Regulation (CRR, June 2013) and the Capital Requirements Directive (CRD, June 2013), Single Supervisory Mechanism (SSM, June 2013) and the Single Resolution Mechanism (SRM, December 2013), while its third pillar, the European Deposit Insurance Scheme is still under discussion (De Rynck, 2016). CRR/CRD has harmonized regulation among EU member states, strengthened specific regulatory agencies within member states (McPhilemy, 2014) and accorded some discretionary powers to national authorities in using a

few macroprudential tools, like the loan-to-value and the debt-to-income ratios (Mérő & Piroska, 2018). The SSM accorded the ECB the right to bank regulation and supervision, including the liquidation of banks. By law, the ECB was granted supremacy over national authorities in politically sensitive areas. This holds especially true in the field of bank authorization where the ECB gained the right to make decisions over bank ownership (Epstein, 2017; Mérő & Piroska, 2018). The SRM changed the bank recapitalization policy and introduced a new bail-in regime, obligating shareholders, bondholders and some depositors to participate in the rescuing of banks (Epstein & Rhodes, 2016; Spendzharova, 2016). Thus, as has been already mentioned, the BU delegated substantial powers to the ECB and designated national authorities.

Figure 1 New European Banking Governance



The figure 1 recapitulates the key political and regulatory characteristics of the NEBG and their influence to reduce democratic oversight of bank restructuring. The NEBG impacts the scope and character of banking policy formation in member states through the following mechanism: First, the NEBG further re-scales states decision-making by transferring

considerable parts of (the remaining) state macroeconomic sovereignty over fiscal, banking and competition policy to non-elected and executive supranational institutions, especially to the ECB, DG-COMP, DG-ECFIN, and the Council of Europe. At the same time, the NEBG impacts internal relations and institutions of member states' polity and creates an executive bias through the empowering of governments and central banks in the restructuring of the financial sector. It also weakens parliaments and other non-governmental actors to effectively influence banking policy. Second, as a macroeconomic tool, the one-size-fits-all approach of the NEBG has contradictory effects on different member states. Third, while the NEBG forms a coherent whole, in certain cases only one or a few of its elements are in effect, not the whole of the NEBG framework. Finally, NEBG as a framework of member states' policy formation represents a more important constraint on peripheral member states than on the more powerful ones.

We see three reasons for the heightened impact of NEBG on the periphery. First, the periphery, especially the southern periphery, was much harder hit by the financial and the sovereign debt crisis, which created ample avenue for NEBG to influence domestic politics. Second, government institutions and businesses in the periphery have less lobby power vis-à-vis EU institutions than those in the core. The rules are the same, but enforcement seems to be very different in the core and in the periphery. In addition, democratic institutions are relatively new and democratic practices are not yet consolidated, especially in the eastern periphery (Bohle & Greskovits, 2012; for Slovenian case see Krašovec & Johannsen, 2016).

Case Study Selection and Methodology

Slovenia, a Eurozone member state since 2007 with the highest GDP per capita in the post-socialist region, is also an exception in the post-socialist region, where economic nationalism supported social welfare provisions and consensual neo-corporatism (Becker, 2016; Bohle & Greskovits, 2012; Lindstrom, 2015). Therefore, Slovenia, not only shares the features of new democratic institutions with small post-socialist countries on the periphery, but some of its domestic economic arrangements resemble the southern periphery. Slovenia is similar to the southern member states in its history of preserving domestic actors and state dominated financial sector that also accumulated significant debt burdens during the 2000s (Becker & Jäger, 2012). For this reason, Slovenia shared with Greece, Portugal, Spain and Italy both the experience of the sovereign debt crisis as well as European institutions' response to this crisis. However, unlike these countries, Slovenia was never brought under the Troika's assistance program, therefore it is the ideal case to study the impact of the European governance structure without the interference of the IMF. As such, Slovenia as a case study is the ideal laboratory to study the impact of the NEBG on the periphery because it corresponds to all three scope conditions under which it is much likely that the NEBG has greater impact on domestic politics of peripheral member states' bank restructuring. Although the findings generalizability remains limited, the Slovene case adds a critical variant to the impact of NEBG on peripheral member states.

We employ an exploratory case study method which allows us to advance theoretical insights into the influence of NEBG on member states' policy formation on the periphery (George & Bennett, 2007). We selected a case that features the most scope conditions under which we expect NEBG to influence domestic politics of banking in eastern and southern member states (Gerring, 2006). Therefore, Slovenia allows the analysis of this process in its most complex form. Since this research aims to review in time the interlinking of the new European banking

governance framework's evolution as a structure within which bank restructuring is enfolded, process tracing seems the most appropriate choice. This is because process tracing is, as defined by Collier (2011, p. 824), "an analytic tool for drawing descriptive and causal inferences from diagnostic pieces of evidence—often understood as part of a temporal sequence of events or phenomena."

In this research, for data collection, we used document analysis of official publications of Slovenian parliament and government and the EU institutions, as well as press reviews of both Slovenian and international English language press. We reviewed publicly available statements made by the EU institutions and domestic actors, experts and government representatives.

Banking Restructuring under NEBG – the Case of Slovenia

Undermined Fiscal Democracy and the Banking Crisis

The outbreak of the crisis revealed not only the weaknesses of the Slovenian banking sector but also that the state's fiscal democracy and sovereignty were significantly undermined when the country needed them the most (Podvršič & Schmidt, 2018). Eurozone membership and domestic corporate-banking indebtedness prevented Slovenian economic actors from accumulating significant foreign exchange loans, typical for the pre-crisis debt accumulation of the other European post-socialist countries (Bohle & Greskovits, 2012). Nonetheless, due to a strong concentration of foreign debt in the corporate sector, Slovenian banks were highly exposed to the cooling of the international financial markets (Kržan, 2014). In 2008, corporate debt-to-equity ratio jumped to 146% while the ratio of the Eurozone average stood at 105%

(Ponikvar, Tajnikar, & Došenović Bonča, 2014). There was an urgent need for policy measures that would address the specificities of the banking crisis and prevent its diffusion to other sectors. However, banking restructuring was since the late 2000s regulated by the NEBG and its key authorities, the EC and the ECB, that were *de facto* parts of the Slovenian crisis policy-making.

The EC's removal of the Maastricht ceiling on public finances, the coordination of the European Economic Recovery among finance ministers (Bieling & Lux, 2014) and the ECB's provisions of liquidity allowed the Slovenian government to implement fiscal stimulus to counteract the severe outbreak of the crisis and prevented the outbreak of a full-blown banking crisis. Nevertheless, they did not address the underlying corporate debt problems. When the Slovenian authorities switched toward an "expansionary austerity", supervised and recommended by the EC and the Council of Europe, the situation in the banking sector rapidly worsened under the pressure of decreased domestic demand (cf. Bole, 2012). The difficulties in reprogramming the debts of many firms, also those operating profitably, acted in turn like a boomerang on banks' portfolios and triggered a massive growth of non-performing loans (NPLs). In 2012, when the NPLs peaked at 15% of total loans and represented almost a fifth of the total economic output, the Slovenian banking system was, according to the OECD (2013, p. 16), among the most impaired ones in the OECD countries with respect to the extent of the deterioration of portfolios. The recapitalization of banks, in turn, rapidly built up public debt that experienced a four-fold increase between 2008 and 2014. Although as late as 2012, the country's public debt, standing at about 54% of GDP, was still below the Maastricht criteria, Slovenia found itself in the middle of the Eurozone crisis turmoil once financial markets started to lose confidence in Eurozone countries. (Kržan, 2014)

The weakening of the Slovenian fiscal democracy under the NEBG did not only aggravate the crisis of the banking sector but also led to an unprecedented political crisis. Much like in the pre-crisis period, the Slovenian population, often under the leadership of trade unions, mobilized strongly each year to contest cuts in public expenditures for social welfare. In fact, while the NEBG allowed Slovenia to increase fiscal expenditures for the banking institutions and to recapitalize them, they did not permit the compensation of those that were most affected by the corporate-banking crisis and winding down of firms. Exceeding 10% in 2013, unemployment reached its highest level after the early 1990s transitional recession. Popular pressure for greater social expenditures was mostly resolved by authoritarian like policy-making, legitimated by a fatalist discourse on the emergency situation and threats on the “Troika intervention”. Already in 2010, when the first round of austerity packages had to be adopted, the Prime Minister of the then center-left, Borut Pahor, who “vigorously defended austerity measures imposed on Greece” (Vobič, Slaček Brlek, Aleksander, Mance, & Amon Prodnik, 2014, p. 92) at meetings of the unelected European Council of the Heads of the Eurozone governments and discussions over the participation of Slovenia in the EFSM, claimed that “we should not wait for the Greek scenario” (Mekina, 2010) to legitimize the unilateral implementation of labor market and pension reforms (Stanojević & Klaric, 2013). When the trade unions called for a referendum campaign against legislative changes, the Pahor administration called upon the Constitutional Court to assess the constitutional character of the implemented reform (Feldmann, 2014, p. 84), arguing that “the financial crisis in Slovenia reached extreme levels and [...] the withdrawal of the reform could prevent the country from exercising its duty to act as a social country and to meet the Maastricht Criteria” (Government Communication Office, 2011).

The Constitutional Court, however, refused the government's demand and in spring 2011, both reforms were rejected at the referendum and withdrawn from the legislation. This provoked the first early elections in the history of independent Slovenia, which took place in late 2011 (Stanojević & Klaric, 2013) and brought a right-wing government into power. In a similar vein as its predecessor, the Janša administration used the threat of demanding the conditional European financial assistance in order to legitimize an increasing encroachment on the procedures of formal democracy and the rule of law (Vobič et al., 2014). Between February and June, the coalition changed thirty-three laws under the “fast track” customs procedure (Vukelič, 2013). Despite protests by NGOs, the anti-corruption commission, and the ombudsman, the Slovenian executive continued to rapidly modify additional seventy laws by the end of 2012, which, among other things, transferred the competences of the state prosecution from the Ministry of Justice to the Ministry of Interior (Mekina, 2012).

This emergency-led “austeritarian” policy-making (Podvršič, 2018) culminated at the end of the year, when the Constitutional Court became an integral part of it. During the autumn months, trade unions and the members of the recently established Positive Slovenia Party (PSP), called for a referendum against the proposed measures to resolve the banking crisis, further detailed below. Whereas the unions' calls were dismissed due to the limits of legality (Dnevnik, 2012), the demand of the PSP was reviewed by the Constitutional Court. This time, the court forbade the referendum, claiming that the gravity of the economic crisis and the state obligations included in the European treaties and intergovernmental agreements had priority over the basic principles of formal democracy. After charges of corruption against the Prime Minister became public, another government change took place, bringing into power a center-left coalition under Alenka Bratušek (PSP).

When assuming power, Bratušek announced that it was necessary to “end the atmosphere of fear [...] In Slovenia there will not be a Greek scenario [...] We will try to re-establish a constructive dialogue with civil society, experts, and social partners” (Delo.si, 2013). However, by that time, the asymmetrical remodeling of state institutions under the NEBG markedly contributed to the further weakening of the trade unions’ powers on dominant economic policy. Although the restructuring of the banks had an important impact on the situation in the corporate sector, and hence, on employees, trade unions were mainly excluded from the banking policy-making. “During the entire post-2008 period, social partners have participated in the work of the tripartite Economic and Social Council [...] But the real influence of the partners, especially the unions, on the formation of policies is almost incomparable to the influence they once had in the 1990s” (Stanojević & Kanjuo Mrčela, 2014, pp. 14-15).

In May 2013, Parliament restricted referendum legislation, “expected to facilitate the introduction of fiscal consolidation measures” (Council of the EU, 2013), as explained by the Council of the EU. Indeed, the fiscal rule removed a powerful regulatory tool that allowed Slovenian societal actors to contest the NEBG’s fiscal restrictions for social expenditures. The “third” crisis government soon lost its legitimacy and credibility. Less than a year after it took power, it was forced to resign. The early 2014 elections were won by the newly established centrist Miro Cerar Party, named after its leader. Despite being a newcomer in Slovenian politics, Prime Minister Miro Cerar remained fully committed to the main policy directions pursued by its predecessors (Stanojević et al., 2016, p. 6).

Nationalization under the Technocratic Rule of the NEBG

The weakening of fiscal democracy under the NEBG's state aid and fiscal restrictions went hand in hand with a greater involvement of the EC-COM, EC-ECFIN and the ECB in Slovenian policy-making. At the same time, Slovenian Ministries of Finance and Heads of Governments actively participated in the discussions over the European crisis regulations and policies at the meetings of the Eurogroup and the Council of the EU. By 2013 it became clear that the Slovenian executive and main financial institutions (Bank of Slovenia, Ministry of Finance) have become a constitutive part of what Oberndorfer (2015, p. 202) described as the "European ensemble of non-elected state apparatuses", based on executive managerialism and technocratic rule.

The NEBG's impact on Slovenia during the Eurozone crisis was not merely related to the pro-cyclical pursuit of the austerity measures, but also to the restriction of competition policy. In fact, when taking a closer look at the 2013 banking recapitalisation process, one can see that the NEBG's state aid rules became one of the main vehicles that allowed the EC and the ECB to directly intervene in the institutional arrangement and policy-making of those troubled peripheral states that were not brought under the formal Troika assistance.

In 2012, the Slovenian government elaborated reforms to restructure the banking sector, developed by the Ministry of Finance, where Dejan Krušec occupied the position of secretary. This staff change was very significant because the government centralised all decision-making powers within the ministry directly linked to international finance. Janez Šušteršič, the minister of finance at the time, explained that the "anti-crisis concept and program" were mostly designed within the cabinet for finance (Marn, 2012). Krušec¹ joined the ECB's team in 2006 and became a member of the IMF/EC/ECB team in 2010. As a representative of the

¹ The information provided here is taken from the following Mekina (2015).

ECB with regard to bank solvency, he participated in restructuring the banking sector in Ireland and Portugal. The restructuring of Irish banks in 2009–2010 was also the model for the strategy adopted by the Slovenian governments. It consisted of creating a separate Bank Asset Management Company (BAMC) or “bad bank” to take over the NPLs in return for government-guaranteed bonds. The financial framework for the operation was based on stress tests carried out by the BS in autumn 2012 in line with the methodological proposals of the IMF mission (Bank of Slovenia, 2013).

Many local experts as well as economists disagreed with this “one-size-fits-all” option, mostly because of its relatively higher public costs and the fact that this mechanism could not by itself resolve the problem of corporate indebtedness, adapted to the Slovenian economy (Kržan, 2014; Ribnikar, 2012; Stošicki, 2011). Those voices were, however, ignored by political authorities, while the calls for referenda were dismissed or forbidden by the government, as mentioned above. Hence, the “Irish” banking solution for Slovenia gained legal grounds with the adoption of the Measures of the Republic of Slovenia to Strengthen the Stability of Banks Act (Official Gazette, No 105/12; ZUKSB), in December 2012, that foresaw the establishment of the BAMC.

The Bratušek coalition, coming into power in 2013, confirmed in its National Reform and Stability Program that it would continue with the restructuring strategy of its predecessor and announced a new recapitalization of banks. This huge fiscal challenge that the Slovenian authorities had to face coincided with a significant upgrading of the NEBG with the “Two-pack” and the launch of the BU that further increased discretionary powers of the EC and the ECB over the Slovenian banking policy formation. The launching of the Two-pack procedure, coinciding with the decision of the EC that Slovenia was experiencing excessive

macroeconomic imbalances (EU Commission 2012), placed Slovenian macroeconomic policies, especially state aid, under the heightened control of the EU executive (Council of the EU 2013, EU Commission 2013a). This implied that the Bratušek government was allowed to recapitalize the main domestic banks only if conformed to the strict European technocratic executism.

During the fiscal coordination cycle in April and May, the EC stopped procedures and, together with the ECB, demanded the BS to produce a new Asset Quality Review (AQR) of banks' portfolios (S. Taškar Beloglavec & Taškar Beloglavec, 2014). As a prerequisite for the approval of state aid, the BS was asked to engage international consultants and real estate appraisers that would ensure the compliance of the methods tested and international standards with comparable reviews previously conducted in countries under the Troika rule (Greece, Portugal, Ireland, Spain, and Cyprus). Moreover, to comply with the recapitalization process with the provisions of the New Banking Communication, the banking legislation regarding the provision of the banking capital and insolvency procedures had to be changed in a very short time. These tasks were realized with a complete compliance of the BS and the Slovenian government that followed the European rule-based policy-making regardless of the potential economic and political consequences.

The so-called independent review of banks' portfolios was carried out on ten banks and banking groups, representing about 70% of the banking system in Slovenia. It was not only a very expensive task but also postponed much needed rehabilitation of the banking sector and came at a much higher estimation of the total capital needs of the banks in comparison to the BS's initial calculations. According to initial calculations, the estimated costs of the recapitalization of the three largest banks were EUR 0.900 billion. In contrast, according to

the ECB directed review, the remaining capital requirement amounted to over EUR 3 billion (Mencinger, Juuse, & Kattel, 2014). In addition, in mid-2013, the Governor position of the central banking authority was overtaken by Boštjan Jazbec, who has constructed a solid network in international finance and its main institutions, like the EBRD, the WB, the BIS, as well as the IMF (Pistotnik & Živčič, 2015). The BS also strongly supported Slovenian authorities when they rapidly and with no public discussion modified the banking legislation to allow for the participation of bank owners and junior creditors in the recapitalization of banks.

The interplay between the NEBG's regulations, the interference of the EC and ECB and the submission of the "Slovenian Troika" to the European technocratic rule led to the result that in 2013, the state recapitalized the main domestic banks to a tune of 10.3% of GDP. In addition, about 3.3 billion of bad assets were to be transferred from the two main banks, NLB and NKBM, to the BAMC (S. Taškar Beloglavec & Taškar Beloglavec, 2014, p. 41). At the same time, under the burden of a costly banking restructuring operation, the central government debt went up from 54% in 2012 to almost 70% of GDP by the end of 2013, and, with rising interest rates, peaked at almost 83% of GDP in 2015 (IMAD, 2014, pp. 22, 23).

Foreign-led Privatization under Strengthened Executives

The 2013 recapitalization process of Slovenian banks is a striking example of Streeck's (2015, p. 366) observation that "[w]here there are still democratic institutions in Europe, there is no economic governance any more [...] And where there is economic governance, democracy is elsewhere." Indeed, in 2014, more than 90% of the population was dissatisfied with the state of democracy, while prior to the crisis, a mere half of the population expressed

similar opinion (Krašovec & Johannsen, 2016, p. 6). In fact, despite the government change in early 2014, the economic stabilization as well as the softening of austerity measures following the European Council's decision from March 2013 to move toward a "growth-friendly fiscal consolidation" (Council of the EU, 2013, p. C 217/275), while the post-state-aid restructuring of banks has been coordinated and supervised by national and supranational institutions.

To get the EC's approval for recapitalization, the Slovenian government had to make several commitments regarding the corporate governance structure of the banks that received public funds. These commitments included, among others, the full privatization of the NKBM by the end of 2016, the reduction of state ownership in the NLB to the 25% plus 1 share by the end of 2017, the merging of the Abanka and Banka Celje, followed by the privatization of the merged Abanka by the end of July 2019 (S. Taškar Beloglavec & Taškar Beloglavec, 2014). These commitments expanded the privatization program adopted by the Parliament in the middle of 2013 which included 15 corporations from strategic sectors, such as the national airport.

In line with the past experience of mass mobilization against bank privatization (Lindstrom & Piroška, 2007), the planned selling of domestic banks provoked multiple forms of resistance. The new left-lined United Left Party (the Left), in opposition during the Cerar administration, warned the public on several occasions that "[t]he Commitments that were given, are not law binding, but are political" (MMC RTV SLO, 2015). The Left actively supported the efforts of the civil society organization "Citizens against privatization!" and joined the petition movement against the privatization, launched by Jože Mencinger, the Slovenian economist known for being among the key designers of the country's gradual transition path. For him "it [was] necessary that Slovenia increase its self-confidence in relation to the European

Commission and we should not silently accept everything that they are imposing on us” (MMC RTV SLO, 2015). According to the public opinion poll conducted in early 2015, 64.5% of participants were against the privatization of NLB (Vičič, 2015).

If not before, then three years later, in August 2018, when the EC approved the new Slovenian privatization plan for NLB (European Commission, 2018), it became clear that the societal actors hardly have any significant impact on the restructuring process. In June 2015, the 100 percent share of NKBM, the second largest Slovenian bank with around 10% market share (European Commission, 2013) was sold to hedge fund Apollo, a branch within Apollo Global Management, LLC that ended up owning 80% of the bank’s shares (Gole, 2015). The launching of the foreign-led privatization in Slovenia also prompted the EBRD to reopen its office in the capital city in January 2014, after an eight-year absence (The Slovenia Times, 2014). In 2015, the EBRD became the second owner of NKBM and acquired 20% of the bank’s shares (Gole, 2015).

The privatization of NLB did not pass, however, so smoothly. In fact, a large share of people arguing against the privatization were supporters of the party of the then Prime Minister (Vičič, 2015). Starting mid-2016, the government tried to delay the privatization process. When at the beginning of 2017, the popularity of the ruling party was rapidly shrinking in favor of the right-leaning Social Democracy Party (MMC RTV SLO, 2017), the government started to send the EC requests for changing the privatization plan. While its first proposal was to divide the privatization into two steps, realized in a two-year period (Jereb Brankovič, 2017), the second one concerned the selling of NLB’s subsidiaries abroad while keeping the bank under state ownership (Žerjavič, 2017). As a consequence, the EC launched an in-depth investigation of the privatization process that was closed in August 2018 with the EC’s

approval of new commitments from the Slovenian government (European Commission, 2018). The summer months revealed that the concrete method and pace of the privatization of NLB became an instrument of the pre-electoral competition for voters of the Miro Cerar Party and the strategy of its leader to shelter himself from the political responsibility of selling the banking group that was one of the key symbols of Slovenian banking nationalist exception during the transition period. It was in the interim period, during the formation of a new ruling coalition, that Slovenian authorities gave a commitment to the EC to sell 75% minus one share of NLB by the end of 2019. The EC announced that “[i]f Slovenia does not respect the deadlines foreseen, a divestiture trustee will be appointed to take over the sales process” (European Commission, 2018).

On November 12, 59% of the bank’s shares have been sold in an initial public offering, making US financial fund Brandes Investment Partners and the EBRD the biggest single institutional buyers of shares detaining 7.6% and 6.3% of the bank’s shares. The remaining state shares of up to 75% minus one share should be sell by the end of next year. The move provoked political criticism, including among the parties in the current government. Nevertheless, except for the Left, there is a shared sentiment among political parties that “Slovenia had to sell the bank since this was a prerequisite for the state aid five years ago” (The Slovenia Times 2018). However, it must be noted that the choice of dispersed ownership (with the government keeping 25%+1 shares) as opposed to selling the bank to one strategic investor, ensures a higher level of government influence over the bank’s business strategy in the future.

Note, the privatization of the bank that was completely owned by the state has long-term negative impacts on the Slovenian fiscal balance, regardless of the one-off revenues related to

the banks' sale that would lower the Slovenian public debt and interest rates. The fiscal balance will lose an important income from the bank's dividends which exceeded EUR 270 million in 2018. Kordež (2018), another important Slovenian economist, estimates that the selling of the bank will worsen the fiscal result by at least EUR 130 million (0.3% BDP).

Again, the realization of this supervision has largely depended on the BS, whose supervisory powers over domestic banks have been considerably upgraded with the establishment of the National Designated Authority under the BU. The Act Amending the Banking Act (Official Gazette, No 105/12: ZBan-1J), in force since November 2013, also granted the BS with new tools to act in cases in which banks run into increased risks (Mencinger et al., 2014, p. 67). The ECB was particularly enthusiastic about the legislation change and welcomed the reinforced role of the BS in banking restructuring (S. Taškar Beloglavec & Taškar Beloglavec, 2014, p. 41).

All in all, the NEBG's macroeconomic and policy restrictions prolonged and deepened the banking crisis in Slovenia, contributed to a costly state rescue that boosted state debt and led to the privatization of the key systemic bank which will have a negative long-term effect on Slovenian fiscal balance. What is more, during the process institutional and political capacities of democratic "invoice" of the Slovenian social actors, known for using their mobilisation capacities to actively participate in banking restructuring in the past, especially as far as the ownership changes are concerned (cf. Lindstrom & Piroška, 2007), were significantly undermined. This implies that there is little chance for a major change in policy direction or a change in the form of policy-making. This could be achieved only if the regulatory framework of the banking restructuring, its European underpinnings and unevenly rescaled character are addressed properly and in a democratic manner.

Conclusion

Using the example of Slovenia, this paper advances a two-fold argument. First, it is argued that one can consider the impacts of the post-crisis European regulations on the restructuring of banks in member states, especially on the European periphery, only by going beyond the BU provisions to include also the supranational changes in other macroeconomic fields. Here, we propose to conceptualize these new developments in a European governance framework as the NEBG. Second, this article argues that the NEBG did not simply reduce the scope of sovereign policy formation but also incited a crisis in the forms and extent of democratic contestation in the European periphery. The structural limitations on the democratic policy making are much more constraining and have far-reaching and longer terms impacts on decreasing democratic oversight of banking policy than just informal pressures and "conjectural" strategies of political elites in power.

The mechanism through which the NEBG works includes the uneven re-scaling of states decision-making by transferring considerable parts of state macroeconomic sovereignty over fiscal, banking and competition policy to the supranational institutions. In addition, the NEBG also impacts domestic politics in member states and creates an executive bias through the empowering of governments and central banks. The NEBG also weakens parliaments, elected politicians, trade unions, and other non-governmental actors' ability to effectively influence banking policy. Because the NEBG does not necessarily deliver economic efficiency, it also weakens the legitimacy of those same institutions, acting on a supranational and national levels. Thus, the NEBG contributes to a situation in which domestic actors increasingly question the policy choices of the EU and governmental bodies, but the efforts of the former

are rebuffed with an enhanced power of the state institutions, connected to the European executive institutions. Hence, the European polity experiences the crisis of democracy.

Studying the banking crisis in Slovenia through the NEBG conceptual framework demonstrates the hollowing out of democratic institutions, the strengthening of the executive, rule-based policy-making and the narrowing of fiscal democracy in banking policy formation in this peripheral EU member state. However, it is important to remind us that the various manifestations of the crisis of democracy on the periphery are not linked in uniform or equal ways to changes in EU's governance structure. Instead, the NEBG's impact is uniquely filtered through each countries' domestic institutions and macroeconomic situation on the periphery.

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